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IN THE

# Supreme Court of the United States

October Term, 1942.

No. 116

LANE-WELLS COMPANY, a corporation, and TECHNICRAFT ENGINEERING CORPORATION, a corporation,

*Petitioners,*

*vs.*

COMMISSIONER OF INTERNAL REVENUE,

*Respondent.*

## PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

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*Respondent.*

## PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT.

Lane-Wells Company, a corporation, and Technicraft Engineering Corporation, a corporation, as your petitioners respectfully pray that a Writ of Certiorari issue to review a judgment entered March 22, 1943, in the United States Circuit Court of Appeals for the Ninth Circuit, in case No. 10183 entitled, "Lane-Wells Company, a corporation, and Technicraft Engineering Corporation, a corporation, Petitioners, vs. Commissioner of Internal Revenue, Respondent." There were originally two cases, but the same were consolidated in the Circuit Court inasmuch as they involved the same facts, and the matters were separate only because there was an assessment against Lane-Wells Company as transferee of Technicraft Engineering Corporation. It will serve the purposes of convenience of this Honorable Court that the cases continue to be treated as consolidated.

## Questions Presented.

1. May the Circuit Court of Appeals affirm a decision of the Tax Court of the United States (formerly the United States Board of Tax Appeals) on the ground that there was substantial evidence to support the decision of the Tax Court, and in support of such action rely upon a conclusion of law rather than a finding of fact?

2. Where the evidence of the taxpayer in the hearing before the Tax Court of the United States proceeds on the legal conclusion that all of the income of such taxpayer was not royalty income within the meaning of the Personal Holding Company Act, and where the decision of the Tax Court, which is affirmed by the Circuit Court of Appeals, adopts a distinction as to portions of that income, would not the accepted and usual course of judicial proceeding require the matter to be remanded to the original trial court for the purpose of permitting the taxpayer to introduce the evidence segregating the income in accordance with the principals determined upon by the Tax Court and affirmed by the Circuit Court of Appeals?

3. Where the findings of the Tax Court are of pure fact, and sustained by substantial evidence, may the Circuit Court of Appeals, in affirming the Tax Court, reverse such findings?

## Statement.

Briefly stated, the facts upon which the foregoing questions arose are as follows: The Commissioner contends that during the calendar years 1934, 1935 and 1936, Technicraft Engineering Corporation (hereinafter referred to as Technicraft) was a personal holding company within the meaning of that term as defined by Section 351 of the Revenue Act. At all times herein involved, all of

the corporate stock of Technicraft was owned in equal amounts by four persons, to-wit, W. G. Lane, Hazel T. Lane (husband and wife) and Walter T. Wells and Mary P. Wells (husband and wife). Technicraft was one of five corporations, the stock of each of which was held in the same manner and in its entirety by Messrs. Wells and Lane and their respective wives [Tr. 150, 151, 164]. At all times herein involved, all of these corporations, with the exception of Technicraft, were engaged in the performance of various skilled, technical services in the oil industry, particularly the service of gun perforating [Tr. 151, 152]. In addition to such rendition of services, all of these related corporations (except Technicraft) were engaged also in the manufacture and sale of various products used in the oil industry [Tr. 152]. At all times after March, 1934, at which time it commenced business operations, Technicraft was engaged in engineering, research, and development work [Tr. 151, 158, 160, 161, 162, 170, 171, 173, 179, 117].

When the business of their corporations was first launched, Messrs. Wells and Lane, both of whom were engineers, were cognizant of the necessity of keeping abreast with scientific developments in the oil industry as essential to the success of an oil service business [Tr. 164, 165]. In December of 1932 they acquired an exclusive license to a patent from one, Sidney Mims [Tr. 118], which patent had been issued in the year 1926 and had never proven itself commercially practicable [Tr. 154, 156, 157, 163, 171, 172, 173, 175, 178]. Foreseeing the need of scientific research and development on the process of gun perforating, which Mims had sought to develop, and seeing also the need of extensive scientific research and development on various other devices and processes

in order to build a successful oil service business, Messrs. Wells and Lane, in December of 1932, agreed that they would set aside 15% of all their income from gun perforating, which 15% would be used to carry on the research, engineering and scientific development of Technicraft [Tr. 164, 165]. Accordingly, Technicraft became a "laboratory" wherein patents or new processes or devices were secured, developed and passed on to the other Lane-Wells companies, which were engaged in services, manufacture and sale [Tr. 158]. In order to provide a convenient method of collecting the 15% of gun perforating income which was to constitute the research fund to be used by Technicraft for the benefit of the various Lane-Wells companies, license agreements were issued from Technicraft to Lane-Wells Company, a California corporation, Lane-Wells Co. of Oklahoma, an Oklahoma corporation, and Lane-Wells Co. of Texas, a Texas corporation [Tr. 165, 166]. It was not the intention of the persons involved that these be true license agreements, but rather than that, the execution of the license agreements constituted a bookkeeping means of providing Technicraft with reimbursement for engineering services rendered [Tr. 171, 173, 176, 261]. The 15% gun perforating income was collected from Lane-Wells Co. of Oklahoma and Lane-Wells Co. of Texas, and the entire system of engineering, research and development continued even after the license agreements had expired in February of 1937 [Tr. 166]. Lane-Wells International, Inc., another of the related Lane-Wells companies, and which was organized in 1936, received the benefits of engineering development by Technicraft and paid 15% of its income, even without going through the formality of execution of a similar license agreement [Tr. 166].

As a result of scientific development and engineering research by Technicraft, gun perforating, which had been commercially impracticable under the Mims patent, became a very successful and profitable business [Tr. 178]. In addition to the developments in gun perforating, Technicraft engineers explored new fields of endeavor in the oil industry and developed and patented many new products, such as fishing magnets [Tr. 162], packers [Tr. 176, 177], bridging plugs [Tr. 180], packing glands, etc. [Tr. 158], and many new services such as Stratagraph [Tr. 160, 161], ex-raying of cable [Tr. 160], underground surveys, etc., all of which were passed on without any further charge to the various Lane-Wells companies [Tr. 166]. Technicraft was not a mere depository for patents, but on the other hand, occupied a large building designed for engineering purposes, in which it carried on extensive and elaborate engineering functions [Tr. 159, 162]. It had on its payroll many experienced engineers [Tr. 179].

The Commissioner contends that Technicraft's income was royalty income within the meaning of the Personal Holding Company Act. The taxpayer contends that form must give way to substance and that the income which Technicraft received as compensation for engineering services is not "royalty" income merely because it was paid through the artificial arrangement of patent license agreements.

The Circuit Court of Appeals for the Ninth Circuit affirmed the decision of the Tax Court on the ground that said court "could reject the testimony of the prior agreements that the furnishing of these patents and models and mechanical devices or processes were mere professional engineering services paid for by the 15% of gross income." The Circuit Court also held that "* * * if,

in addition to the licensed matter, non-royalty devices were given for the same 15% consideration, there was no segregation to show that they amounted to over 20% of the taxed income." In the first instance, the Circuit Court ignored the fact that the Tax Court did not "reject" the testimony of the prior agreements, but, on the contrary, by its express findings, recognized the existence of a prior agreement that the furnishing of the patents and models and mechanical devices and processes were mere professional engineering services paid for by the 15% gross income. Apparently the Circuit Court mistook the Tax Court's conclusion of law to the effect that the income was royalty income for a finding of fact. In the second instance, by its decision, the Circuit Court of Appeals defeated the ends of justice by not affording to the petitioners, by proper remand to the Tax Court of the United States, an opportunity to evidence the segregation between the sources of income that would reveal that unquestionable non-royalty income sources constituted more than 20% of the petitioners' taxed income. It is in consequence of said judgment and act of said Circuit Court of Appeals that your petitioners seek review by certiorari in this Honorable Court to determine that a litigant's rights may not be summarily destroyed by the failure of a Circuit Court to distinguish between findings of fact and conclusions of law; and to determine also that where a case has not been adequately tried so as to cover issues developed for the first time on appeal therefrom, that said matter should be remanded so that a litigant may enjoy his day in court on all issues properly presented to the trial court.

## Reasons Relied Upon for the Allowance of the Writ of Certiorari.

It is respectfully submitted by your petitioners and relied upon as reasons for the granting of the writ that:

1. The act of the Circuit Court of Appeals for the Ninth Circuit in confusing findings of fact and conclusions of law has the effect of being a departure so far from the accepted and usual course of judicial proceeding as to call for an exercise of this Court's power of supervision.

2. The act of the Circuit Court of Appeals in assuming that the Tax Court had rejected testimony, when in fact the Tax Court had based its findings upon the truth of such testimony, is of such materiality as to leave the decision of the Circuit Court without any support whatsoever.

3. The decision of the Circuit Court of Appeals upholds a decision of the Tax Court of the United States, which is based upon the theory that the petitioners should have introduced evidence segregating classes of income, and justice would require the matter to be remanded to the Tax Court so that evidence of such segregation could be presented to the Tax Court for consideration.

4. The decision of the Circuit Court of Appeals has the effect of reversing the findings of fact of the Tax Court despite the fact that such findings are of pure fact and are supported by substantial and competent evidence. In reversing the findings of the Tax Court, that are supported by competent evidence, the Circuit Court has adopted a procedure in conflict not only with its own decisions, but the decisions of other Circuit Courts and the controlling decisions of the United States Supreme Court.

Wherefore, your petitioners respectfully pray that a Writ of Certiorari be issued out of and under the seal of this Honorable Court, directed to the United States Circuit Court of Appeals for the Ninth Circuit, directing that Court to certify and send to this Court for its review and determination, on a day certain to be therein named, a full and complete transcript of the record and all proceedings in the case numbered and entitled on its docket as No. 10183, "Lane-Wells Company, a corporation, and Technicraft Engineering Corporation, a corporation, Petitioners, vs. Commissioner of Internal Revenue, Respondent," and that the judgment of said Court be reversed by this Honorable Court and that your petitioners may have such other and further relief in the premises as to this Honorable Court may seem meet and just.

June, 1943.

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